HOW MEETING COMPLIANCE MANDATES CAN CREATE BUSINESS VALUE

By aimpublications LLC

"Current compliance strategies are faced with an increasing challenge of scale, complexity and overlap," says Sandeep Vishnu, managing director at BearingPoint.

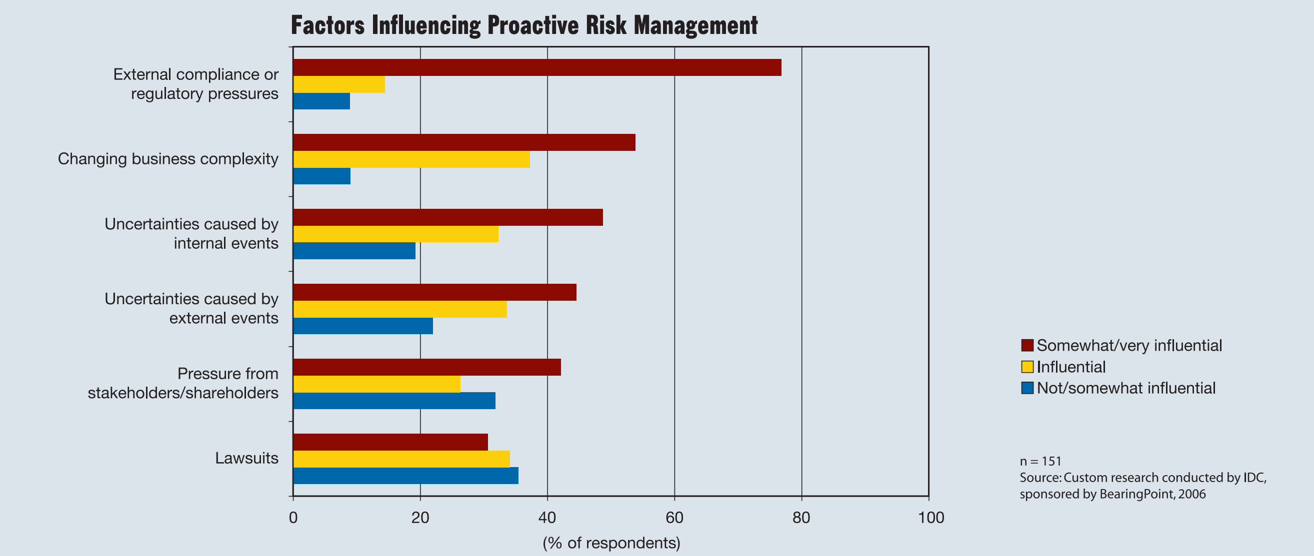
The scope of the changes mandated by compliance requirements — ranging from the Federal Information Security Management Act of 2002, OMB 123 and the Revised International Capital Framework (or Basel II), to the Patriot Act and, perhaps most notably, the Sarbanes-Oxley Act of 2002 — is so sweeping that companies are feeling the need to be more proactive in managing risk.[i]

Developing and implementing a strategy for meeting compliance mandates drives immediate value. Implementing a holistic strategy to manage all enterprise risk drives long-term value. When considered within the context of overall risk management, compliance mandates can yield benefits through the capture and reuse of compliance data and through merging disparate, piecemeal risk and compliance efforts into a more complete and anticipatory risk management framework that includes compliance mandates as minimum requirements.

Addressing Compliance Creates Business Value

Companies can derive business value in three key areas when they take a holistic approach to meeting compliance mandates. First, they will see improvements in risk management practices. They will also enjoy better return on investment and enhanced uses of technology. The specific benefits achieved by addressing compliance in this kind of holistic fashion include:

- *Avoiding losses* by reducing fines and litigation;
- *Cutting regulatory and compliance costs* both in the form of



lower infrastructure costs and fewer associated audit costs;

- *Boosting business performance,* including improved decision making and processes, increased flexibility in launching or terminating growth initiatives, and aligning resources with these initiatives;
- *Reducing costs by providing a means to avoid unnecessary risks* as a result of marginalizing risks that are significant;
- *Improving a company's strategic position* by enabling the creation of competitive advantage in situations where a risk domain is better understood relative to the competition;
- *Enhancing market capitalization* by improving investment returns across growth initiatives with sophisticated risk management techniques, including hedging and use of financial derivatives;
- *Augmenting sustainable competitive advantage* needed to support business goals and financial objectives by enabling proper resource and investment allocation based on risk and return.

Compliance, Risk and Corporate Strategy: Examples to Remember

How companies address compliance and risk issues can have a powerful impact on strategic direction, investment opportunities and technology decisions. For instance:

Market-facing and organizational factors. **The cost of failure to identify the risks involved in moving into new global markets is illustrated by one global bank's multimillion-dollar fine for violating U.S. foreign-trade regulations and anti-money-laundering laws.**[ii]

Seemingly minor events can grow large indeed under media scrutiny. One large U.S. pharmaceutical company's failure to disclose the health risks of one of its best-selling products may have forever changed the nature of its relationship with its customer base.

Influence on investments and growth alternatives. **A globally diversified bank had to rethink M&A posture when the Federal Reserve Bank questioned its integration and financial operations compliance programs.**

Today's Risk Is Tomorrow's Regulation: Managing Risk Can Reduce Compliance Efforts

Linking compliance mandates and the governance paradigm with an overall risk management strategy is quickly becoming a corporate must-have, and for good reason. Ill-managed risks often become mandates with the goal of getting companies to manage them appropriately.

"Today's risk is tomorrow's regulation," notes Tony Klimas, managing director at BearingPoint. "Properly understanding and managing risk can not only reduce the overall effort of compliance, it can actually generate business value from this reduced effort."

Better information, more efficient and effective business processes and more successful execution of corporate strategy can all be derived from meeting the linked mandates of compliance, governance and risk management. Done well, such an effort can even create strategic differentiation, enabling an organization to successfully pursue strategies with inherently more risk — and more return.

"At some level, many regulatory requirements address fundamental flaws in the way businesses are run and ultimately in how shareholder value is created," Klimas points out. "Responding to regulatory requirements with an approach that links these requirements to business improvement and business value — essentially to the ability to execute strategic intent — will ultimately result in better-run businesses and improved shareholder value."

Investing in a New Perspective

In too many organizations today, compliance functions are still reactive and siloed. Part of the problem, observes Ronald Diel, managing director at BearingPoint, is that "most companies will continue to be forced to implement point solutions for certain regulations, such as HIPAA."

Such point solution investments should, however, be the beginning of their compliance efforts — not the end. It's important to understand the

Compliance Costs: Higher and Higher

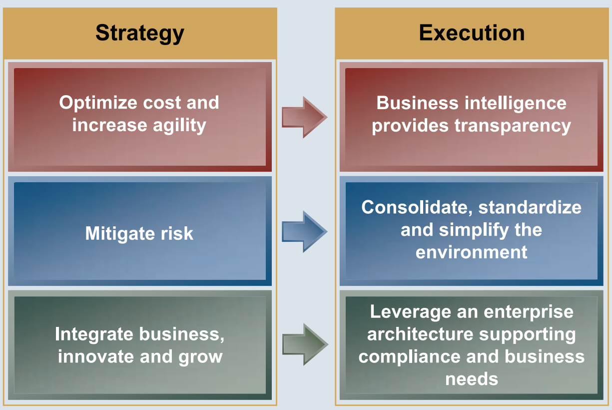
When Gartner asked what percentage of the IT budget was being spent on compliance, more than 1,400 CIOs estimated, on average, 12%. When this same group was asked to predict what that IT share would be in 2009, the answer was 14.2%.[iii]

And, of course, today's compliance costs reach far beyond the IT department. Companies must spend on additional auditors as well as legal and regulatory experts. The cost of employee time — that of line managers, CIOs, CFOs and CEOs — adds up too. No wonder the U.S. Securities Industry Association has reported that in the past three years, compliance costs just for the securities industry have nearly doubled to $25.5 billion.

limitations of a point solution. "Instead of looking for ways to fundamentally change the organization's approach to regulatory and compliance issues," says Klimas, "many companies are caught up in the moment, spending vast sums of money on a recurring basis, treating the symptoms instead of the problem."

The good news is that fundamental change does not necessarily come from investing in new products, but rather from investing in a new perspective that links compliance and risk priorities with strategic objectives.

Take a Holistic Approach to Managing Risk and Compliance



Source: BearingPoint, 2006

Compliance mandates can create business value in three very powerful ways:

- *Holistic management of risk, compliance and strategy:* Regulatory compliance issues will grow, but by taking an integrated approach to risk management, companies will be in a better position to manage those compliance factors in a more streamlined and cost-effective manner.

  "By developing an integrated strategic approach towards compliance," Diel advises, "you help your point solutions meet both regulatory and corporate objectives, and ultimately reduce the time and cost needed to complete these solutions through economies of scale and reusable components. A moderate expenditure on planning and structure can have sizable benefits later."
- *Improved ROI:* By streamlining compliance activities across the organization and standardizing data and technology, the enterprise will be able to successfully reduce operational costs and improve investment decisions.

  Diel points to the importance of defining and using standardized communications interfaces. Even companies forced to build point solutions "can create an environment in which those systems are later tied together in a more holistic way by using standard messages shared across an enterprise-wide service bus," he says.
- *Leveraging existing technologies:* Though redeploying technology seems expensive and time-consuming, the alternative — inaction — inevitably leads to delays or workarounds in support of new initiatives. An examination of existing tools and applications often yields ways to reuse already-available technology to support the organization's needs for efficient risk and compliance management as well as its continuing strategic development.

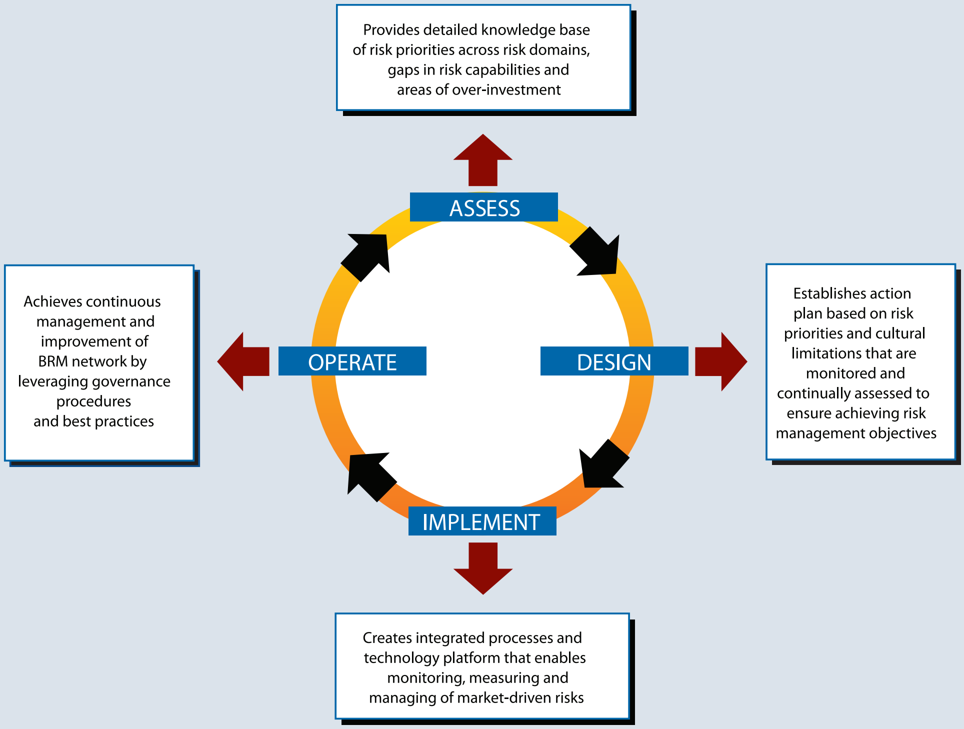
Holistic Risk Management: Steps to Linking Compliance To Your Corporate Strategy

Inevitably, compliance becomes costly for companies that haven't taken advantage of the opportunity to proactively implement risk management techniques. Compliance strategies should be designed and implemented based on the enterprise's assessment of its risk priorities to achieve compliance objectives. Such a design must do the following:

- *Deliver an integrated risk and compliance management solution* that can be implemented throughout the *entire* enterprise;
- *Include a customizable risk model* that addresses specific enterprise pain points involving both compliance and risk issues;
- *Combine risk management with technology-savvy process-driven improvements* and be repeatable, flexible and able to respond quickly.

Even before addressing technology considerations, creation of an effective business risk management framework that addresses compliance issues involves a number of key leading practices:

BearingPoint's Business Risk Management (BRM) Framework



An integrated framework is critical to successfully managing all types of risks disrupting daily operations and execution of strategy. BearingPoint's approach starts with a Business Risk Management (BRM) Framework, offering a risk model to assess the cost and impact of business risks; then designs and implements strategies for achieving each risk management objective with standard, repeatable approaches supported by governance, operations, processes and technology. To operate effectively, the framework should be updated with metrics, processes, investments, etc. that keep an organization in alignment with rapid changes in the market. Source: BearingPoint, 2006

- Ensuring executive buy-in across strategic corporate officers (CXOs) and business line managers;
- Evaluating your company's culture, boundaries and risk tolerance levels to determine the types and extent of the risks it can manage;
- Assessing risk options — which risks should be avoided, reduced in significance or accepted and monitored as part of normal business operations — and reprioritizing key business enablers and risk factors with an eye to external issues, then aligning them with business objectives, strategy, processes and performance-driven metrics;
- Building in an initiative to increase employees' risk awareness;
- Using a variety of risk-related information sources, including trained risk management professionals, experts in the field and risk owners;
- Developing an enterprise-wide compliance and risk management language and using it;
- Providing trained risk management professionals skilled in specific industries and domains.

Once a company's risk tolerance has been evaluated and risks have been prioritized, an action plan can be constructed. This describes the organizational, policy and procedure, process and technology changes needed to support an effective compliance and risk management environment and enables risks to be assigned to domains based on source, impact, resources and business objectives.

Finally, by implementing a monitoring and review cycle, companies can ensure action plans meet established goals and can identify areas for compliance and risk management improvements.

Improving ROI: Simplify, Standardize and Consolidate To Reduce Ever-Increasing Operational Costs

Most organizations never realize the full potential of the data available to them. Often they are unable to integrate that unfiltered data across the organization and into information that can be used for decision making.

By integrating compliance and risk information and embedding compliance controls, companies can do much more than simply comply. They can create competitive advantage in the form of more accurate analytics, better understanding of their business cycle and the ability to interact with the capital markets using information that is produced faster and more accurately.

Companies that understand the implications of integration are shifting their focus to automated controls. These have enabled firms to simplify processes, standardize and centralize, resulting in much lower back-office operating costs.

Responding to the fundamental need for integrated information does not necessarily mean starting all over. Before investing in tools, program change or enterprise applications, it's worthwhile to:

- Identify what needs to be measured;
- Examine data quality and security;
- Study feedback loops to evaluate results and change the organization's focus;
- Train management to approach risk proactively.

Consider the experience of one large North American bank that has always monitored its results using technology that tracks productivity and error rates to drive down defect rates and discover sources of potential processing errors. With the imposition of Sarbanes-Oxley, the bank unit was well prepared for the changes it would bring, since its structured management process already provided almost all review-control needs. Any incremental items were identified and satisfied with some adjustments to existing data-gathering tools.

The bank's key to success: a clear understanding of the regulatory risk within the context of the overall risk environment and the ability to match this understanding, in the form of requirements, to existing technology capability.

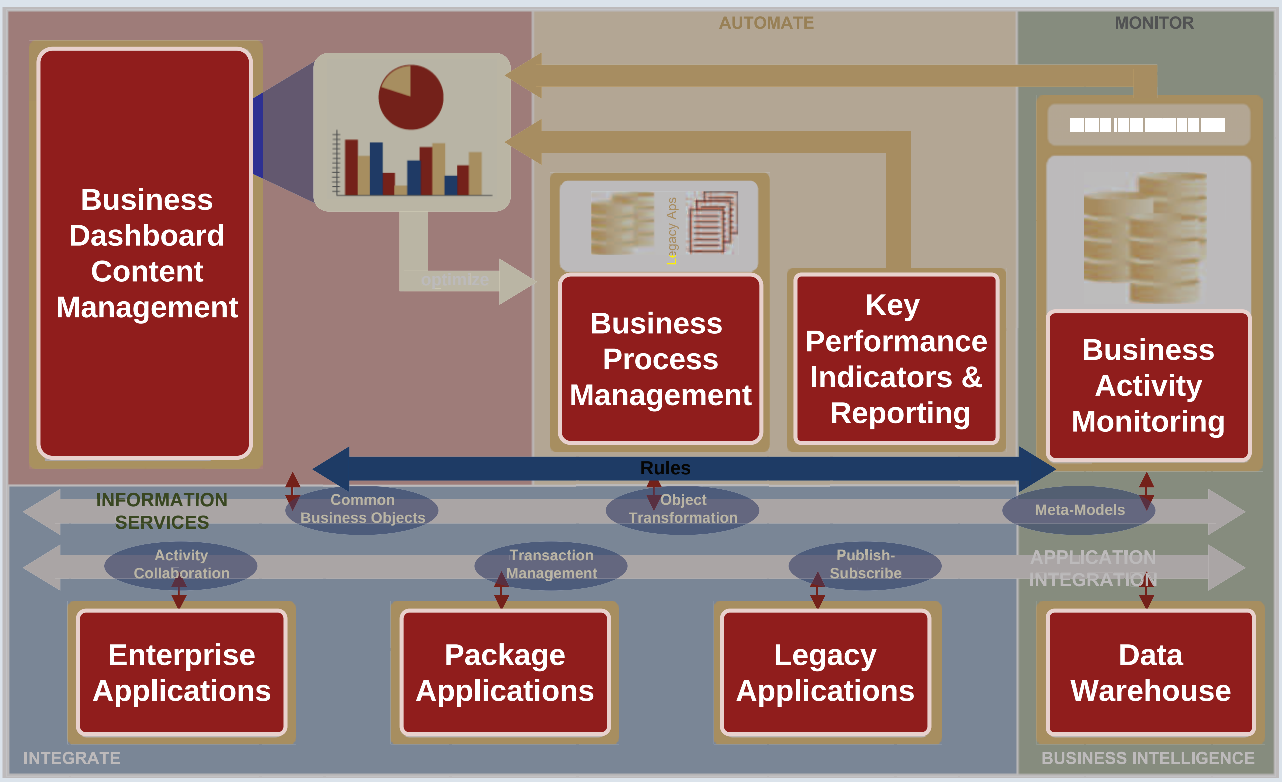
Leveraging Current Technology Investments for Enterprise-wide Compliance and Risk Management

"More advanced firms have now begun to adopt a longer-term architectural approach that holds out the promise of lower spending over time and a more flexible, more capable compliance and risk management environment," says Ronald Diel.

The technologies used to enable compliance and risk management processes must address a variety of requirements in support of several key goals. Tony Klimas describes these requirements:

- A way to assess and capture all sources, impacts and domains for risk and compliance. You then need to link these to strategic objectives, assessing such factors as importance and performance as well as organizational capability to manage risk and compliance. This includes capture of risk levels such as inherent risk and tolerable risk, and also must allow for continuous periodic assessment;

Accept the Challenge of Reusing Current Technology



Source: BearingPoint, 2006

The Technologies Behind Compliance and Business Risk Management

Only by connecting all of an organization's risk domains can a cross-silo, converged view of compliance activities and exposures be achieved. Here's what it takes:

- **A means by which business application information and workflow management messages can be distributed and shared (an enterprise service bus [ESB]);**
- **Coordinating automated and manual procedures that require processing across multiple business areas and systems (workflow management tools and standards);**
- **A way to drive business-specific activities across the workflow managers, including control activities engines that insert legally mandated control activities into the workflow and then monitor and report their performance (business process support applications);**
- **An effective and consistent solution to the increasing requirements for security and privacy protection (a standardized authentication and identity management layer);**
- **A single integrated compliance database that provides the information required for all compliance-specific applications, standard reports and filings; an ad hoc query tool tailored to compliance needs; a compliance dashboard that groups information about compliance issues, business processes, cases being resolved and regulatory schedules with appropriate security controls and drill-down tools; and a search engine that can access and filter records in the compliance database.**

- A means to capture action plans for each prioritized risk and compliance mandate, tracking progress, including metrics, for monitoring achievement of stated goals;
- A mechanism that maintains and communicates the various responsibilities and owners of the compliance and risk management process;
- An ability to manage and communicate information about the compliance and risk management process;
- A searchable repository for compliance and risk management data and documents;
- An ability to monitor and disseminate process information related to compliance and risk management;
- Linkage between compliance and risk management information and business information for analysis and reporting.

Fortunately, in many organizations, current technology investments can be leveraged in support of such efforts. Thus holistic, enterprise-wide compliance can in turn be leveraged to meet both the day-to-day business and strategic needs of corporations as well as adapt to evolve with changing business requirements in a range of industries, from financial services and telecommunications to utilities and manufacturing.

For example, out of concern that some pharmaceutical companies may have inappropriately influenced healthcare provider (HCP) prescribing habits, many states require life-science companies to track and report on all payments to individual HCPs. Since the business processes and internal systems of most life-science organizations have a wide range of payment transactions, this requirement poses a significant data management challenge.

Rather than developing and deploying a single-focus HCP compliance solution, many leading pharmaceutical companies are leaving existing transactional systems in place and adding a risk monitoring solution. The solution's business intelligence tools collect and report data and capture control documents, while its business process management tools manage and track HCP payment approvals.

By leaving existing best-of-breed applications in place, companies can more efficiently integrate risk management into existing business processes rather than layering on additional processes and systems. The result: increased operational efficiency and business risk reduction.

What to Do Next

"The bottom line here," says Tony Klimas, "is to not simply throw dollars after compliance point solutions, but rather to first understand the overall context in which these solutions will be used. Done right, significant savings can be achieved — especially if compliance systems can be built around existing architecture."

Begin with a commitment to continuous planning. This will help to avoid unnecessary complexity and multiple disparate solutions that instantly devolve to legacy status. Organize compliance efforts in phases:

- *Short-term,* a comprehensive risk assessment can help properly define the compliance environment and create a common language for dealing with this environment. It will enable you to identify and prioritize risks — including compliance risks — and design action plans outlining a strategy for managing each risk and compliance mandate.
- *Long term,* you'll need to build a business risk framework — including a technology architecture and the proper tools for managing compliance across the enterprise and a governance structure for continuous operation of risk and compliance management.

In successful organizations, investments in compliance, risk assessment and information technology will be undertaken not only with an eye to meeting regulatory requirements, they will simultaneously be regarded as investments that enhance root business processes across the entire enterprise and support the organization's strategies and goals.

To do otherwise is not only too costly, it also means that key strategic opportunities will be missed. ■

Written by aimpublications LLC (www.aimpublications.com), provider of editorial and analytic consulting focused on technology and business issues and trends.

[i] *Understanding Business Risk Management: Achieving Optimal Growth and Performance.* Custom research conducted by IDC, sponsored by BearingPoint, authored by Monica Huber, 2006.

[ii] *Dutch Bank Fined for Iran, Libya Transactions $80 Million Levied for Foreign Dealings, Money Laundering,* by Paul Blustein, *Washington Post*, December 20, 2005.

[iii] Gartner Report: *Understanding the Costs of Compliance*, John Bace et al, July 7, 2006.